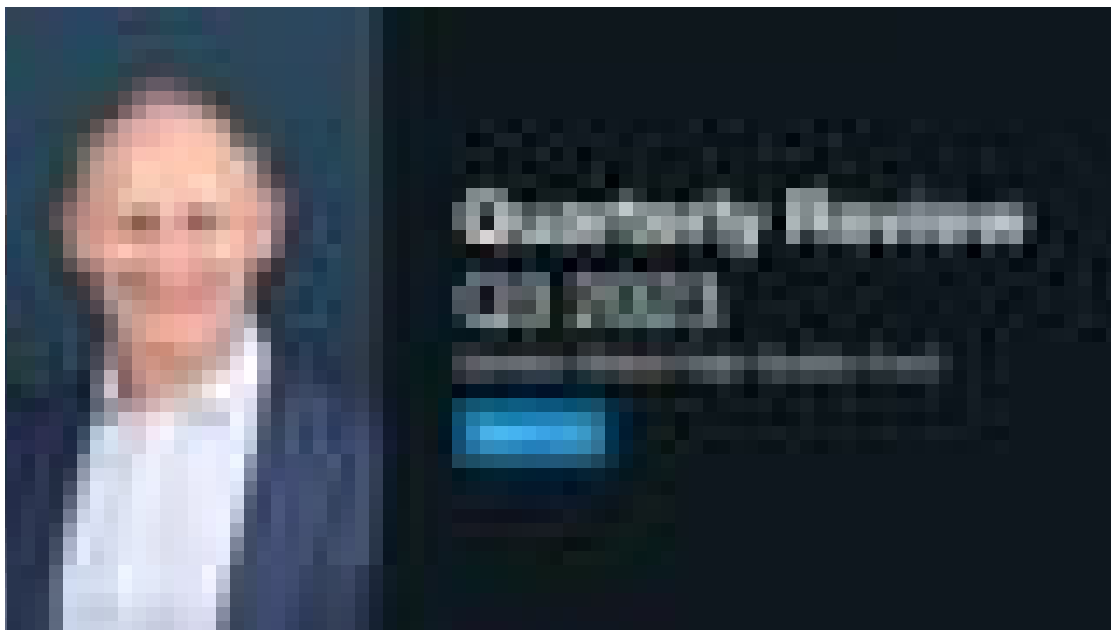


Sanlam Global High Quality Fund Quarterly Review - Q3 2023

Chris Rodgers is joined by Head of Global Equities, **Pieter Fourie**, who provides an overview of the Sanlam Global High Quality Fund's performance, current market trends, and an outlook for the future.



You can also read our [quarterly investment update here](#).

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Full transcript

Chris Rodgers

Good morning. My name is Chris Rodgers. I'm head of investments here at Sanlam Investments UK in London. And with me this morning is Pieter Fourie. Pieter is head of our global equity team and the lead manager on the Global High Quality Fund. And this morning, we're going to talk about the third quarter of 2023. Morning, Pieter.

As always, markets seem uncertain and particularly volatile at the moment. How have you found the third quarter?

Pieter Fourie

I think it's a very exciting time, Chris. If you look at what's actually worked this quarter, it's been energy stocks. Some of the trends that we've seen last year has re-established itself. So the US is back in favour. The dollar's very strong and some of the sectors that we've been adding to quite aggressively is performing very well this year.

So it's really technology, communications and consumer discretionary driving the market forward and the volatility

and some of the vicious underperformance we've seen in parts of Europe has actually allowed us to make some very interesting changes in the portfolio, which we're really excited about.

Chris Rodgers

Okay. So perhaps we will delve into some of those new ideas, new holdings in the funds.

Pieter Fourie

Yeah. So a good, good example is Heineken. So we've seen a big under-performance from quality companies in Europe. It's something we've warned about for a while that if we if we look at, say, an Alphabet and a Microsoft and the valuations of those names a year ago versus Rémy Cointreau or Diageo or a Heineken, we thought that you get a lot of potential upside in some of those US names.

Now, when the narrative was quite negative around these companies, whereas, you know, the growth outlook for some of the European staples companies were really weak for the multiples you were paying and suddenly you just saw quite a big collapse in something like Heineken, a stock that we've owned three and a half years ago, close to the lows in the market panic and a stock that's now on the same level as seven years ago.

But the earnings power is about 50% higher. It's just a convoluted way of saying it offers very good free cash flow yield now 7%, if you look out 2 to 3 years from now for very steady growth and that's why we've been buying that in the portfolio on the back of this massive sell-off in some of the names in Europe.

Chris Rodgers

And how would you fund that? Have you been taking profits in some of the more richly priced areas of the market?

Pieter Fourie

Yes, that's a good point. And I think it's that's why we're very encouraged about also when we look back now at the performance, we are ahead of the peer group year to date, one year, three year. But it's been a very, you know, volatile journey, so to speak. Back in May of 2020, we were buying very lowly rated businesses like Novartis, Swiss Pharmaceutical Company, and that one's actually, along with Intuit, has been some of our best performers since the market sort of went into a what so far as a bear market from the beginning of last year.

So that stock and a name like Intuit, we've done 30 to 40% and against that, you actually had big laggards in Heineken, so whereas for the one we see 30% upside to intrinsic value, Novartis was trading very close to fair value, um, quite a predictable business, but also it does have patent rights and issues that Pharms always have.

So we decided, you know, in terms of much more upside in Heineken, we decided to sell Novartis.

Chris Rodgers

The whole entire holding?

Pieter Fourie

We sold the entire holding yes you know, at this stage the only pharmaceuticals we have left is Johnson and Johnson, which has been an old and long-term holding. And we also have Roche. It's interesting, Roche is now at a big discount to Novartis and it was very different three years ago and we're still quite confident about the pipeline in that business.

But we have in effect reduced our pharmaceutical positions and by buying back into Edwards Lifesciences, having sold that in June, we saw 30% pullback. We did think at the time at 3% free cash flow yields too expensive. We didn't know the market's going to fall out of love with healthcare, particularly on the growth side. So that's also one that we've invested in and we've

Chris Rodgers

Gone back into that one?

Pieter Fourie

We've gone back into the fund is essentially fully invested at the moment and we're quite excited about a 5.6% free cash flow.

Chris Rodgers

And you touched on Intuit, was that a just a trim or a disposal?

Pieter Fourie

No. So we so we're keeping Intuit.

Chris Rodgers

It's just one that you've got your eye on has done quite well.

Pieter Fourie

Yeah. We've invested in that in May and I think it's in May of last year. Yeah. And, and it's, it's, I think it's important to note that many, many names like Edwards Life and Heineken in fact and Intuit. The entry points are very important if you look back over two year or three year period, some of these stocks have returned negative returns, but we've had very good outcomes.

Yeah, so the volatility is playing into our hands. We like that we've got a set universe of names we don't stray from. And I think it's important to know the companies on your watchlist very well. So for Intuit, when it did go to about 500, we brought it back slightly from about 3% to 2.5%.

So it's quite fully valued today, but I think they're very well positioned for the AI themes that we are excited about.

Chris Rodgers

It sounds as though you're being quite adept on the trading front, even though you've got your eye on the longer term.

Pieter Fourie

Yeah, I think it's, it's, it's if you think about the if you think about Microsoft or even a stock like NetEase, it's almost doubled from October last year. Yeah. When China was way out of favour. So I think if you have 60 70% moves in a year from things like Microsoft and Alphabet, of course, that does change your assessment of where how much you should own.

So whereas we were buying in March, a lot of Microsoft at 350 we did trim it, so we did take it back from 5 to 3.8, but we do like the long-term, the long-term compounding effect of those names. So we will be active around the positions, but only because it's so volatile out there.

Chris Rodgers

Sounds as though you're enjoying the volatility. Yes. So what is performance? It's been quite a respectable quarter, albeit not without its challenges. You touched on oil. You don't hold any oil stocks. So that must have been a bit of a headwind.

Pieter Fourie

It was a headwind in the last month of the quarter and September, basically in line with the market in September, slightly ahead for the quarter but we were down, I think it was three and a half in dollars versus 3.7 for the market. So we are behind about two and a half percent this year, year to date as of today.

But we're very happy if we look at the path that we followed the last year and the last three years, it looks very different to our peer group. And we don't, of course, you know, care about the peer group per se, but the path that we followed was a realistic outcome. We always tried to be realistic with our return expectations.

We bought great businesses when they offered value and now we are making quite a few changes where our assessment has changed on that outcome. But if you look if you look at some of the big drivers of performance this year, like Microsoft and Google, I think it's important Alphabet, rather it's important to note that they you know, they have been going sideways for the last two years.

So we're excited that below those mega caps we can find the Heinekens the Edwards Lifes the Thermo Fishers of the world and selectively also, you know, the Samsungs of the world that we've owned for more than a decade in our strategy on and off. And now we think those are the kind of names that can take the portfolio forward.

Chris Rodgers

As you say. I mean, I think albeit slightly behind over the year to date, that's pretty respectable. And we know that it's been a challenging market for active managers given the narrowness of the leadership. And that does make it more difficult. So how are you positioned going forward? You mentioned some of the names. Are there any strong sector tilts in the portfolio?

Pieter Fourie

Well, we are you know, there's been some sector changes this this year from a classification point of view. So if we were to look at, you know, names like Visa and Pfizer in the portfolio on the payments side, if you take that and also on two new exchange positions, relatively new exchange positions in London Stock Exchange Group and Intercontinental Exchange, even though those four stocks are classified as financials, we believe that it's the technology behind what they doing, the data services they provide, the security services they provide in the case of Visa, that some of those names have been very long-standing positions.

Pieter Fourie

So between financials at 15% our communications exposure and things like Electronic Arts, which is which is which looks to us as if the value is very compelling at this stage after three years of sideways movement. So between communications technology and financials, which we really look at as tech companies, it is about, you know, 40 to 50% of the portfolio.

And then we combine that with some of our favourite sort of franchise businesses like Yum Brands and Intercontinental Hotels Group. And you know, another good example of a stock that's finally delivered for us in a big

way this year, 30%, it's up 40% over three years, you know, and a lot of investors fell out of love with that, thinking that the business model is failed or that people will never stay in a hotel again.

And you know, those sort of companies, the algorithms are the same, it's very high return on equity businesses. The portfolio's on 5.6% free cash flow yield. It's right in the middle of the long term range for us. And we're very excited about the spread of business as we have.

Chris Rodgers

As a bottom up stock picker. I know you don't pay excessive regard to the macro outlook, but we still have a framework. What's your best guess as to where we go from here? Do you think we can entirely avoid a recession in the US?

Pieter Fourie

Yes, I think, you know, you're always going to be careful about your own biases. I've always been quite bullish about the dollar, about the US, etc. but you have to marry that with a large valuation premium in the US. You know, if you think about maybe a recession around the dawn and everybody's been wrong so far, is Europe really going to come out of that better than the US?

I don't think so. So what we have seen, and that was my view for a while, is that if investors are scared about a recession in Europe, they did flock to the Coloplasts and the Novo Nordisks of the world and some have done really badly and some of them have done really well from a share price point of view, but they're all quite expensive.

So I think it's there's no point positioning yourself with a macro view where the market already has positioned themselves into those names. And you know, for the record, I do believe we're going into a slowdown. We've had massive fiscal stimulus which has been different in this cycle. We've got huge pressure on bond yields going up which means that equities are less attractive from that point of view.

But we can't control those macro factors. What we can control, though, is to be very assertive when we think stocks have overreacted. Yeah.

Chris Rodgers

Okay. That's a fantastic overview, Pieter, that I think has given our viewers and listeners a good insight into the portfolio. But if you have any questions that you'd like to put to Pieter, please in the first instance, speak to your Sanlam representative and we will relay those questions to Pieter and get back to you. Thank you very much indeed.